



REPORT OF EXAMINATION

EAGLE PACIFIC INSURANCE COMPANY

As of December 31, 1996

*Prepared for the
Washington State Insurance Commissioner's Office
by Examiners Peter Mendoza, Martin Severeid, Larry Omdal and Leman
McClean, Chief Property/Casualty Actuary D. Lee Barclay, and
Actuarial Assistant Jim Antush
810 Third Avenue, Suite 650
Seattle, WA 98104*

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify that the attached Report of Examination shows the financial condition and affairs of EAGLE PACIFIC INSURANCE COMPANY of Seattle, Washington, as of December 31, 1996.

Chief Examiner

Date

EAGLE PACIFIC INSURANCE COMPANY
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Seattle, Washington
September 1, 1998

The Honorable George M. Reider, Jr.
Commissioner, State of Connecticut Insurance Dept.
Chairman, NAIC Financial Condition (EX-4) Sub-Committee
P.O. Box 816
Hartford, Connecticut 06142-0816

The Honorable Christopher P. Krahling
Superintendent of Insurance, State of New Mexico
NAIC Secretary, Western Zone
P.O. Drawer 1269
Santa Fe, New Mexico 87504-1269

The Honorable Deborah Senn
Commissioner, Washington Insurance Department
Insurance Building, AQ-21
Olympia, WA 98504-0255

Dear Commissioners:

In accordance with your instructions and in compliance with the statutes of the State of Washington (RCW 48.03), an Association Examination has been made of the corporate affairs and financial records of the

EAGLE PACIFIC INSURANCE COMPANY
of
Seattle, Washington

hereinafter referred to as the Company, at its home office located at 4025 Delridge Way SW, Seattle, Washington 98106. The following report on examination is respectfully submitted showing the condition of the Company as of December 31, 1996.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 1991. The current examination was conducted by insurance examiners from the State of Washington and covers the period from January 1, 1992 through December 31, 1996. The examination was conducted in accordance with the laws and regulations of the State of Washington contained in Title 48 of the Revised Code of Washington and Title 284 of the Washington Administrative Code and the examination procedures recommended by the National Association of Insurance Commissioners found in the NAIC Financial Condition Examiner's Handbook.

Corporate records and various aspects of the Company's operating procedures and financial records were reviewed and tested during the course of this examination and are commented upon in the following sections of this report. The Company's Certified Public Accountant's work papers were reviewed and utilized where possible to support efficiency in the examination.

Comments on any adverse findings which are applicable to the current examination are included in the Instructions and the Comments and Recommendations sections of this report.

INSTRUCTIONS

Pursuant to the findings and conclusions of the examiners, the Company is hereby instructed to comply with the following:

1. **THE COMPANY IS INSTRUCTED** to comply with **RCW 48.05.280 Records and Accounts** of insurers, which requires that: "Every insurer shall keep full and adequate accounts and records of its assets, obligations, transactions, and affairs."
2. **THE COMPANY IS INSTRUCTED** to comply with **RCW 48.07.040 Annual, special meetings**, which requires that, "Each...insurer shall...hold the annual meeting of its shareholders...for the purpose of receiving reports of its affairs and to elect directors." Article II, Section (2) of the Corporate Bylaws specifies that the date of the annual meeting shall be the last Thursday in April. Article IV, Section (1) of the Corporate Bylaws specifies that the term for directors shall be for one year.
3. **THE COMPANY IS INSTRUCTED** to comply with **RCW 48.13.340 Authorization of investments**, which requires that, "No investment...be made...unless authorized or approved by its board of directors or by a committee... The minutes of any such committee shall be recorded and reports thereof shall be submitted to the board of directors for approval or disapproval."
4. **THE COMPANY IS INSTRUCTED** to comply with **RCW 48.13.350 Record of investments, Section (1)** which requires, "...a written record in permanent form showing the authorization... "Section (2) which requires, "...records shall contain: (b) In the case of securities: (reference details of security)"

COMMENTS AND RECOMMENDATIONS

Pursuant to the findings and conclusions of the examiners, it is recommended:

1. **IT IS RECOMMENDED** that in addition to those items of business already being included in the Board of Director Minutes, (such as changes to Articles of Incorporation and Corporate Bylaws, Authorization for Capital changes, Dividend Declarations, Appointment of Actuary and Conflict of Interest Statement Acknowledgment) the following items of business should also be included: Authorization for Director and Officer Compensation, Authorization for Bonus Compensation, Expansion of the Territory of Business (i.e. Certificates of Authority obtained), and Appointment of Certified Public Accountant.
2. **IT IS RECOMMENDED** that beginning with the 1998 Annual Statement, the Company calculate and record in Schedule P, Part 1, Columns 19 and 20, appropriate amounts for bulk and IBNR reserves for allocated loss adjustment expense. (In the 1996 Annual Statement, these amounts appear to be included with losses unpaid, in Columns 15 and 16.

HISTORY

The Company was incorporated under the laws of the State of Washington on June 7, 1978 to write Workers' Compensation insurance in both the State Act and the United States Longshore and Harbor Workers market. In 1981, the Company changed ownership and moved its administrative office from Bellevue, Washington to Waukesha, Wisconsin.

On August 6, 1982, Stevedoring Services of America, Inc. (formerly Seattle Stevedore Company) purchased all of the outstanding stock of the Company and the administrative office was then relocated to Seattle, Washington.

On February 1, 1985, Stevedoring Services of America, Inc. made a capital contribution of \$12,873,978 to the Company. The capital contribution consisted of 100% of the stock of Hanseatic Eastern Insurance Company, Ltd. and Executive Insurance Company, Ltd. of Hamilton, Bermuda. On February 7, 1986, Stevedoring Services of America, Inc. changed its name to Stevedoring Services Group, Inc., and then on August 20, 1986 to Services Group of America, Inc.

Eagle Insurance Group, Inc. was formed in April, 1987 as a holding company for the insurance and insurance service related operations of Services Group of America, Inc. On April 30, 1987, all of the outstanding stock of the Company was contributed to Eagle Insurance Group, Inc.

In 1983, the existing inforce premiums and all of the outstanding reserves of Executive Insurance Company, Ltd. were transferred to Hanseatic Eastern Insurance Company, Ltd. which had been previously transferred to the Company in 1985. In December, 1990, Executive Insurance Company, Ltd. was liquidated.

In July, 1991, all of the outstanding liabilities of Hanseatic Eastern Insurance Company, Ltd. were assumed by the Company and Hanseatic Eastern Insurance Company, Ltd. was liquidated in December 1991.

CAPITALIZATION:

In September 1992, during the period covered by this examination, the Board of Directors authorized a change in the par value from \$400 per share to \$810 per share. At December 31, 1996, there were 6,500 shares of authorized common capital stock of which 6,500 shares were issued and outstanding. All shares are owned by Eagle Insurance Group, Inc., an insurance holding company domiciled in the State of Washington. Thomas J. Stewart is the ultimate controlling person through an upstream relationship of companies.

HISTORY (Continued)

DIVIDENDS TO SHAREHOLDERS:

The Company distributed shareholder dividends during four of the five years under examination to the one shareholder, Eagle Insurance Group, Inc. The total amount distributed, or \$24,200,000 was made from available surplus funds derived from net realized profits as required by RCW 48.08.030. None would be considered extraordinary dividends.

The following is a schedule of the dividends paid during the examination period. These amounts were authorized by the Board of Directors and so noted in the Board of Directors meeting minutes.

<u>Year</u>	<u>Amount Paid</u>	<u>% of Assets</u>
1992	\$14,000,000	8.49%
1993	\$ 0	0.00%
1994	\$ 3,500,000	2.05%
1995	\$ 3,000,000	1.71%
1996	\$ 3,700,000	2.01%

AFFILIATED COMPANIES

Eagle Insurance Group, Inc. was formed in April, 1987 as the holding company for the insurance and insurance service related operations of Services Group of America, Inc. The Company is a wholly owned subsidiary of the holding company. As a member of a holding company system, holding company statements are required and have been filed on an annual basis with the Washington State Insurance Commissioner's Office showing the subsidiaries of Eagle Insurance Group, Inc. and the ultimate controlling person.

Pacific Eagle Insurance Company was incorporated under the laws of the state of California on September 1, 1988. The company is only admitted in California and writes state act workers' compensation coverage. Many of these policies are companion policies for the USL&H policies written by Eagle Pacific Insurance Company.

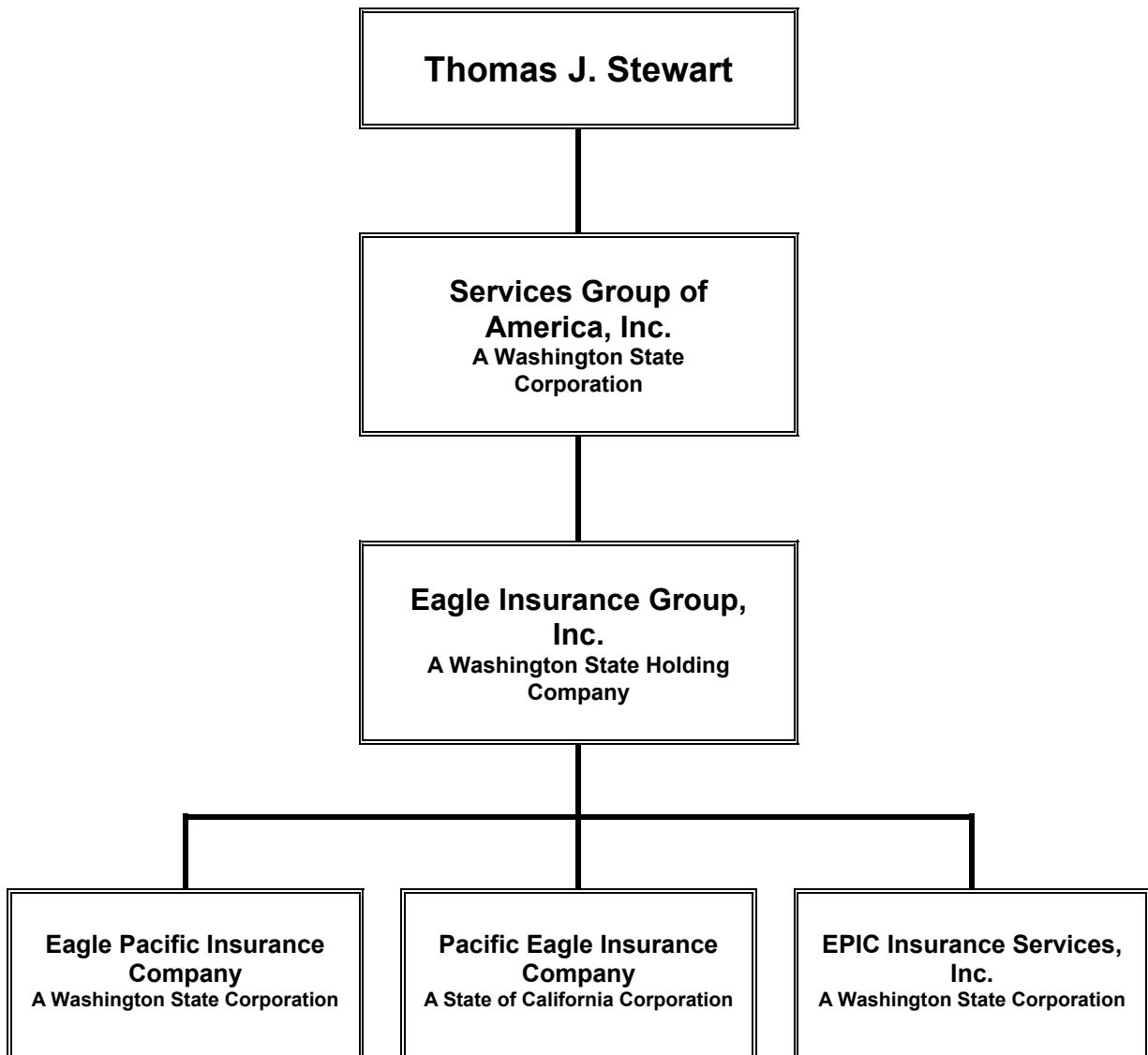
EPIC Insurance Services, Inc. was incorporated under the laws of the state of Washington on May 15, 1984. EPIC provides administration of workers' compensation claims for self insured employers in Washington, Hawaii, Alaska, and Oregon. It is also a licensed agency in Washington state. EPIC will be withdrawing from the majority of its third party administration work in 1998 as its book of business has been sold to Intermountain Claims of Boise Idaho.

Costs are allocated to Pacific Eagle under the terms of a quota share reinsurance agreement. EPIC pays for most of its expenses directly, but certain reimbursements are made to Eagle Pacific for administrative and computer usage costs. All of the companies are under a tax sharing agreement by which they remit taxes to the parent company on a basis of what they would have owed the IRS on a stand alone basis.

An organizational chart of Eagle Insurance Group, Inc. follows on the next page.

ORGANIZATIONAL CHART

The following displays the upstream relationship of the various entities of the Eagle Insurance Group to their ultimate parent.



MANAGEMENT and CONTROL

The Articles of Incorporation were amended three times during the period of examination.

Article IV of the Articles of Incorporation was amended, changing the par value of the common capital stock to \$810. Article X of the Articles of Incorporation was amended to remove specific requirements for number, qualifications, term of office, manner of election, time and place of meeting, and powers and duties of the directors from the Articles of Incorporation because those terms are included in Article IV of the Corporate Bylaws. Article IV, Section 1, 2nd sentence of the Corporate Bylaws was amended, changing the number of Directors from four to three. All of these were amended in a special meeting of the Board of Directors on September 30, 1992.

Article IX was amended August 19, 1994 making the principal office of the corporation; 4025 Delridge Way S.W., Suite 500, Seattle, Washington 98106.

BOARD OF DIRECTORS:

Article IV, Section 1 of the Corporate Bylaws authorizes three directors with whom all matters concerning the management of the Company is vested. Directors are elected for a term of one year, and hold the office until a successor is elected and qualified.

Directors serving the Company at December 31, 1996 were:

<u>Name and Address</u>	<u>Principal Business Affiliation</u>	<u>Director Since</u>
Thomas J. Stewart Vashon Island, Washington	Services Group of America, Inc.	1982
Lawrence A. Riggs Medina, Washington	Services Group of America, Inc.	1986
Dennis J. Specht Mercer Island, Washington	Services Group of America, Inc.	1982

OFFICERS:

Article V, Section 1 of the Bylaws provides that the officers of the Company shall be elected by the Board of Directors for a one year term at their annual meeting held immediately after the annual shareholders meeting. These officers are a Chief Executive Officer, a President, one or more Vice-Presidents, a Secretary and a Treasurer.

Officers on December 31, 1996 were:

R. Steven Clark, Chief Executive Officer and President
John R. Snyder, Executive Vice President
Edward A. Lopit, Vice President
Thomas J. Stewart, Secretary
Greg M. Stevenson, Treasurer

MANAGEMENT and CONTROL (Continued)

COMMITTEES:

Article IV, Section 10 of the Bylaws provides that the Board of Directors may designate from among its members an Executive Committee and one or more special committees. The Executive Committee and the Board of Directors appear to be one and the same, therefore, no special designation of a committee has been made. An Investment Committee was appointed by resolution of the Board of Directors January 2, 1990.

CORPORATE RECORDS:

Article II, Section (2) of the Corporate Bylaws requires that the annual meeting of shareholders be held the last Thursday in April. Section (3) specifies an agenda that should be followed. Generally, regular meetings of the Board of Directors may be held anytime without notice at the principal place of business. The Board of Directors annual meeting is also held without notice, but is required to be held immediately after the adjournment of the annual meeting of shareholders.

The last written record of an election of directors at an annual shareholders meeting was April 25, 1991. One director was removed by shareholder action in a special meeting of shareholders on July 1, 1992. The absence of shareholder meeting minutes creates the appearance that annual meetings are not held and that directors are not elected annually. (See Instructions 1 and 2)

Board of Directors minutes reflect an election of a new Chief Executive Officer and President effective April 16, 1995. Board of Directors minutes of January 20, 1997 also reflect the election of four officers. The last written record of an election prior to this examination period was April 25, 1991. The absence of Board of Directors meeting minutes creates the appearance that annual Board of Directors meetings are not held and that officers are not elected annually. (See Instructions 1 and 2)

During the period covered by the examination Board of Director meeting minutes did not reflect authorization for Director and Officer Compensation, authorization for an annual Bonus Compensation payment, authorization for expansion of the Territory of Business (i.e. Certificates of Authority obtained) or engagement of a Certified Public Accountant. (See Comments and Recommendations 1)

There are no recorded minutes of an Executive Committee or the Investment Committee. In the case of the Investment Committee, the absence of meeting minutes gives the appearance that meetings are not held and a record of investments in report form are not made part of the Investment Committee minutes. (See Instructions 1,3 and 4)

However, the Board of Directors, on June 25, 1997 ratified all investment transactions occurring during the examination period by resolution. The Board, "RESOLVED, that all investments, loans, sales and exchanges thereof and other actions made or taken on behalf of this corporation by this corporation's Investment Committee appointed by resolution of the Board dated January 2, 1990, have been distributed at least monthly to each member of this Board of Directors, are reviewed by each Director and discussed with the Investment Committee as

MANAGEMENT and CONTROL (Continued)

deemed appropriate and necessary, and are properly reflected in this corporation's audited financial statements and annual reports submitted to the Washington State Insurance Commissioner, for the periods ending December 31, 1992 through 1996, and are hereby ratified, confirmed and approved in all respects."

The last ratification prior to this was July 31, 1992 for the period January 1, 1990 through December 31, 1991.

In summary, records of the proceedings of the annual Shareholders' meeting, the Board of Directors' meetings, and the meetings of the Committees of the Board do not exist or do not contain essential authorizations or discussions of decisions reached.

However, it was demonstrated during the planning stages of the examination through interviews with an officer, several managers and the completion of various internal control questionnaires (Ref. SRA Exam File # 4.2), that all Directors and Officers take an active role in the administration of the affairs of the Company. Meetings and discussions are held often among those responsible for making management and investment decisions. All areas of management appear to be aware of what each other is doing and their personal responsibilities towards the goals of the Company.

CONTRACTS

As of December 31, 1996, the Company was a party to the following contracts:

Intercompany Tax Allocation Agreement:

The Company's Federal Income Tax Return is consolidated with the return of its ultimate parent, Services Group of America. Income taxes are allocated as if each affiliate filed a separate tax return. In the event that the Company has net losses, the Company will be credited on a current basis. Periodic payments are made to the parent for any tax liabilities.

Management Agreements:

The Company has agreed to provide management and claim services for an affiliated insurer, Pacific Eagle Insurance Company. Unallocated loss adjustment expenses and out-of-pocket expenses incurred are borne by each party and proportioned to the cost and amount of time and personnel expended by each with respect to such matters.

INTERNAL SECURITY

Conflict of Interest:

The Company has a Conflict of Interest Policy. The Board of Directors, Officers and other employees in positions of responsibility annually complete a conflict of interest disclosure statement and questionnaire. These are presented to the Board of Directors for their acknowledgment.

No conflicts have been disclosed that would indicate a failure to give an undivided and unselfish loyalty to the Company which requires that there be no conflict between duty and self interest.

INTERNAL SECURITY (Continued)

Fidelity Bond and Other Insurance:

The Company is a named insured on a Fidelity insurance policy purchased by the upstream parent, Food Services of America, Inc. Coverage limits to \$5,000,000 are provided after a \$25,000 deductible. This amount of coverage is greater than the NAIC minimum recommendation for a company the size of Eagle Pacific Insurance Company.

The Company is also provided protection against certain property and liability losses as a named insured on policies obtained by its parent, Eagle Insurance Group, Inc. Policies in effect at December 31, 1996 provided coverages for property, boiler and machinery, commercial general liability and auto, excess liability, workers' compensation, excess workers' compensation and crime insurance. Errors and Omissions coverage only applies to the Company Loss Control Department.

The Company does not have Directors and Officers Liability insurance protection because it does not feel at risk.

EMPLOYEES' BENEFIT PLANS

As an affiliated company of Services Group of America, Inc., the Company is able to provide its employees and their dependents with medical, dental, vision care and life and disability benefits.

The Company maintains a defined contribution profit sharing plan covering substantially all employees. The amount of the annual contribution is at the Company's discretion. The Company's contribution expense for the year ended December 31, 1996 was \$453,783.

Employees are also participants in a salary bonus compensation program and are also eligible to participate in a savings plan. They may also on a voluntary basis contribute a portion of their salary to the savings plan.

Employees also receive vacation benefits and may receive educational assistance.

TERRITORY AND PLAN OF OPERATION

Eagle Pacific Insurance Company writes Workers' Compensation insurance in both the State Act and United States Longshore and Harbor Workers (USL&H) markets. The Company was authorized to transact property and casualty business in the states of Alaska, Arizona, Hawaii, Oregon, Utah and Washington. During the period of examination Certificates of Authority were obtained to transact the same types of business in the states of Alabama, Idaho, Louisiana, Texas and the territory of Guam. It is the intent of the Company to seek admission to do business in California and Nevada within the next three years.

Under the terms of its certificate of authority with the federal government, administered by the Department of Labor, the Company writes USL&H risks in the states of Alaska, California, Oregon and Washington.

The following schedule shows the Company's direct writings for the year 1996:

Alabama	0
Alaska	7,506,131
Arizona	317,359
California	4,456,529
Hawaii	22,064,274
Idaho	1,091,728
Louisiana	8,897,563
Oregon	3,493,019
Texas	362,528
Utah	803,077
Washington	3,461,499
Guam	0
TOTAL	52,453,707

At December 31, 1996, the Company utilized the services of approximately 40 independent brokers and agents. These producers were selected based on their specialized skills in handling products underwritten by the Company.

Stevedoring Services of America, Inc. the Company's largest single account (approximately 20% of total), was terminated August 1, 1992. This volume was replaced by expanding operations in other regions, however, overall premium volumes have shown little growth during the period under examination.

The Company has service offices throughout the regions where it conducts business. These offices provide underwriting, loss control and claims servicing. The following is a list of offices by location and the services provided:

Anchorage, Alaska	Claims & Loss Control
Irvine, California	Claims & Loss Control
San Diego, California	Underwriting, Claims & Loss Control
Portland, Oregon	Claims & Loss Control
Seattle, Washington	Underwriting, Claims & Loss Control
Spokane, Washington	Claims

REINSURANCE PROGRAM

Reinsurance Assumed:

The Company assumes risk under a quota share (pooling) agreement with its affiliate, Pacific Eagle Insurance Company. The Company assumes 100% of Pacific Eagle's writings and then retro-cedes 17.5% back to Pacific Eagle.

Reinsurance Ceded:

The Company has three reinsurance programs to protect itself from excessive losses.

Statutory Treaty Coverage of \$49.5 million in excess of \$500,000 is provided through the following reinsurance partners:

<u>Name</u>	<u>Year Joining Program</u>
Odyssey Re	1990
Transatlantic Re	1985
Scor Re	1992
Kemper Re	1995
Zurich Re (UK)	1991

Maritime Employers Liability Excess, \$100,000 retention, \$1,000,000 limit.

Industrial Aid Excess of Loss Reinsurance, use of aircraft coverage, \$250,000 retention, \$10,000,000 limit.

ACCOUNTING RECORDS AND INFORMATION SYSTEMS

The principal accounting systems in use by the company are LAN based, "off the shelf" software programs that have had no modifications made to them. They are stable, mature systems that have been in use at the Company for many years.

Platinum is the primary system used for General Ledger and Accounts Payable. It was developed by Platinum Software, a leader in middle market accounting systems. Investment accounting for marketable securities is performed using Sungard Parex. This system produces NAIC annual statement investment schedules and other management reports. The claims system is an Oracle based client server system that was built in-house and deployed in the fall of 1997. The policy system is a mainframe based system that is scheduled to be replaced by a client/server based system later in 1998. Other programs being used are as follows: Fixed Assets - FAS2000, Investments - Par-Ex, Payroll - Ceridian Payroll Service and Report Writer - Frx.

All of the programs and data files are stored on a file server in a secure computer room. The data files are backed up and stored off site every night.

UNPAID LOSSES AND LOSS ADJUSTMENT EXPENSES

The reserves carried by the Company for these liabilities were \$70,013,463 and \$10,688,053, respectively, as of December 31, 1996.

These reserves were reviewed by the casualty actuarial staff employed by the Washington State Office of Insurance Commissioner. The Company provided loss and loss adjustment expense development data. The OIC actuarial staff obtained additional information by interviewing several Company employees. They also reviewed an actuarial report prepared by the Company's consulting actuarial firm, Milliman & Robertson, Inc.

The OIC actuarial staff's estimates indicate that reserves for losses and loss adjustment expenses combined, both gross and net of reinsurance, are within a reasonable range. Therefore, these reserves are accepted as they appear in the Company's 1996 Annual Statement.

Amounts for bulk and IBNR reserves for allocated loss adjustment expense in the 1996 Annual Statement appear to have been included with losses unpaid in columns 15 and 16. These amounts are more appropriately reported in Schedule P, Part 1, Columns 19 and 20. (See Comments and Recommendations 2)

SUBSEQUENT EVENTS

Ownership and Control:

Lumbermens Mutual Casualty Company has entered into a Share Purchase Agreement with Services Group of America to acquire control of Eagle Pacific Insurance Company. Form A "Statement Regarding the Acquisition of Control of or Merger With a Domestic Insurer" was filed with the Washington State Office of Insurance Commissioner during May 1998 and acquisition was approved by the OIC, July 8, 1998.

Territory and Plan of Operations:

The Company has continued to grow in the Southeast, primarily in Louisiana and Texas USL&H markets. During 1997, a claims and loss control service office was opened in Lafayette, Louisiana. Admission was gained in Alabama in late 1996 and in Mississippi in 1997. Significant activity in those states won't begin until sometime in 1998.

During the first quarter of 1997, the Company closed its Concord, California office. Service for those Northern California accounts has been moved to the Newport Beach, California office. Newport Beach now acts as the regional service office for the Company. The Portland, Oregon office moved its location in the fourth quarter of 1997.

Management:

There have been no changes in key management.

On April 14, 1998, Amendment No. 1, Form B was filed with the Washington State Insurance Commissioner's Office to inform the department of specific litigation and/or administrative proceedings relating to certain Directors and Officers of Eagle Pacific Insurance Company. These actions were specific to alleged federal and state campaign law violations. These proceedings were settled on March 18, 1998 through agreements reached with the various agencies.

SUBSEQUENT EVENTS (Continued)

Policies:

The Company had begun to underwrite mid-size accounts written on guaranteed cost policies during 1996. This shifted the concentration in the book of business from primarily larger loss cost rated accounts to a balance with mid size guaranteed cost accounts. Since the examination date, no single large account lost has materially impacted the Company.

Medical Bill Review:

The Company entered into an agreement with Health Care Compare. HCC will provide the Company with medical bill review services.

Systems:

The Company converted to a new claims management system during August 1997. The system was developed internally. The Company feels that the system is working well and provides improved work flows and more information that will also expedite future examinations.

Reinsurance:

Reinsurance treaties were renewed without significant changes from the prior year.

Financial:

Shareholder dividends of \$4,400,000 were paid to the Company's sole shareholder during 1997. Bonus Compensation paid during February 1997 was \$1,341,700 and February 1998 was \$1,458,500.

These disbursements were ordinary and usual to amounts paid in the years under examination.

FINANCIAL STATEMENTS

The following statements reflect the financial condition of the Company as of December 31, 1996, as determined by this examination:

Balance Sheet
As of December 31, 1996

Statement of Income
Year Ended December 31, 1996

Capital and Surplus Account
As of December 31, 1996

Comparative Balance Sheet
As of December 31, 1995 and 1996

Comparative Statement of Income
For the Years Ended December 31, 1995 and 1996

Comparative Capital and Surplus Account
Years Ended December 31, 1992 through 1996

EAGLE PACIFIC INSURANCE COMPANY

BALANCE SHEET AS OF DECEMBER 31, 1996

	BALANCE PER COMPANY	EXAMINATION ADJUSTMENTS	BALANCE PER EXAMINATION	Notes
<u>ASSETS</u>				
Bonds	\$93,968,218		\$93,968,218	1
Stocks:				
Preferred stocks				
Common stocks	7,562,861		7,562,861	2
Real estate: Properties occupied by the company	12,539,855		12,539,855	3
Cash on hand and on deposit	2,550		2,550	
Short-term investments	16,864,620		16,864,620	4
Other invested assets	476,604		476,604	
Foreign Currency - Futures Contract	2,127,592		2,127,592	5
Agents' balances or uncollected premiums:				
Premiums in course of collection less ceded reinsurance	4,307,142		4,307,142	6
Premiums booked but deferred and not yet due	21,159,899		21,159,899	6
Accrued retrospective premiums	8,067,650		8,067,650	6
Funds held by or deposited with reinsured companies	11,896,958		11,896,958	7
Bills receivable, taken for premiums	199,223		199,223	
Reinsurance recoverable on loss & loss adj. expense pmts.	882,936		882,936	
Electronic data processing equipment	694,706		694,706	
Interest, dividends and real estate income due and accrued	1,881,112		1,881,112	
Receivable from parent, subsidiaries and affiliates	1,146,434		1,146,434	
Total Assets	<u>\$183,778,360</u>		<u>\$183,778,360</u>	
<u>LIABILITIES</u>				
Losses	\$70,013,463		\$70,013,463	8
Loss adjustment expenses	10,688,053		10,688,053	8
Other expenses (excluding taxes, licenses & fees)	3,348,302		3,348,302	
Taxes, licenses & fees (excl. fed. inc. tax)	1,725,472		1,725,472	
Unearned premiums	34,507,369		34,507,369	
Funds held by company under reinsurance treaties	15,768,186		15,768,186	
Amounts withheld by company for others	3,094,873		3,094,873	
Provision for reinsurance	450,000		450,000	
Payable to parent, subsidiaries and affiliates	4,031,000		4,031,000	
Outstanding checks	158,698		158,698	
Total liabilities	<u>143,785,416</u>		<u>143,785,416</u>	
<u>SURPLUS AND OTHER FUNDS</u>				
Common capital stock	5,265,000		5,265,000	
Gross paid in and contributed surplus	11,100,048		11,100,048	
Unassigned funds (surplus)	23,627,895		23,627,895	
Surplus as regards policyholders	<u>39,992,943</u>		<u>39,992,943</u>	

Total liabilities, surplus and other funds	<u>\$183,778,359</u>	<u></u>	<u>\$183,778,359</u>
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EAGLE PACIFIC INSURANCE COMPANY
STATEMENT OF INCOME
YEAR ENDED DECEMBER 31, 1996

	BALANCE PER COMPANY	EXAMINATION ADJUSTMENTS	BALANCE PER EXAMINATION	Notes
<u>UNDERWRITING INCOME</u>				
Premiums earned	\$50,749,215		\$50,749,215	
DEDUCTIONS:				
Losses incurred	24,817,305		24,817,305	
Loss expenses incurred	10,793,341		10,793,341	
Other underwriting expenses incurred	13,978,183		13,978,183	
Total underwriting deductions	49,588,829		49,588,829	
Net underwriting gain or (loss)	1,160,386		1,160,386	
<u>INVESTMENT INCOME</u>				
Net Investment Income earned	7,421,236		7,421,236	
Net realized capital gains or (losses)	1,494,717		1,494,717	
Net investment income gain or (loss)	8,915,953		8,915,953	
<u>OTHER INCOME</u>				
Net gain or loss				
from agents' or premium balances charged off	(385,750)		(385,750)	
Finance and service charges				
not included in premiums	30,805		30,805	
Miscellaneous interest income	33,236		33,236	
Total other income	(321,709)		(321,709)	
Net income before dividends to policyholders and before federal and foreign income taxes	9,754,630		9,754,630	
Dividends to policyholders				
Net income before federal and foreign income taxes	9,754,630		9,754,630	
Federal and foreign income taxes incurred	3,257,363		3,257,363	
Net income	\$6,497,267		\$6,497,267	
Surplus as regards policyholders, December 31, previous year	\$38,252,952		\$38,252,952	
<u>GAINS AND (LOSSES) IN SURPLUS</u>				
Net income	6,497,267		6,497,267	
Net unrealized capital gains or (losses)	91,012		91,012	
Change in non-admitted assets	(1,257,288)		(1,257,288)	
Change in provision for reinsurance	109,000		109,000	
Dividends to Stockholders	(3,700,000)		(3,700,000)	
Changes in surplus	1,739,991		1,739,991	
Surplus as regards policyholders, December 31, current year	\$39,992,943		\$39,992,943	

EAGLE PACIFIC INSURANCE COMPANY
COMPARATIVE BALANCE SHEET
AS OF DECEMBER 31,

	<u>1996</u>	<u>1995</u>
<u>ASSETS</u>		
Bonds	\$93,968,218	\$93,045,590
Stocks:		
Preferred stocks		493,500
Common stocks	7,562,861	2,950,762
Real estate: Properties occupied by the company	12,539,855	12,952,518
Cash on hand and on deposit	2,550	2,400
Short-term investments	16,864,620	19,527,978
Other invested assets	476,604	1,014,966
Foreign Currency - Futures Contract	2,127,592	434,286
Agents' balances or uncollected premiums:		
Premiums in course of collection less ceded reinsurance	4,307,142	12,595,877
Premiums booked but deferred and not yet due	21,159,899	17,837,167
Accrued retrospective premiums	8,067,650	6,819,200
Funds held by or deposited with reinsured companies	11,896,958	3,027,040
Bills receivable, taken for premiums	199,223	815,549
Reinsurance recoverable on loss & loss adj. expense pmts.	882,936	611,015
Electronic data processing equipment	694,706	856,785
Interest, dividends and real estate income due and accrued	1,881,112	1,875,389
Receivable from parent, subsidiaries and affiliates	1,146,434	312,804
Total Assets	<u>\$183,778,360</u>	<u>\$175,172,826</u>
<u>LIABILITIES</u>		
Losses	\$70,013,463	\$75,378,993
Loss adjustment expenses	10,688,053	9,722,631
Other expenses (excluding taxes, licenses & fees)	3,348,302	1,521,151
Taxes, licenses & fees (excl. fed. inc. tax)	1,725,472	2,085,433
Fed. and foreign inc. taxes (excl. def. taxes)		131,627
Unearned premiums	34,507,369	43,267,641
Funds held by company under reinsurance treaties	15,768,186	91,959
Amounts withheld by company for others	3,094,873	3,544,979
Provision for reinsurance	450,000	559,000
Payable to parent, subsidiaries and affiliates	4,031,000	
Outstanding checks	158,698	616,460
Total liabilities	<u>143,785,416</u>	<u>136,919,874</u>
<u>SURPLUS AND OTHER FUNDS</u>		
Common capital stock	5,265,000	5,265,000
Gross paid in and contributed surplus	11,100,048	11,100,048
Unassigned funds (surplus)	23,627,895	21,887,904
Surplus as regards policyholders	39,992,943	38,252,952
Total liabilities, surplus and other funds	<u>\$183,778,359</u>	<u>\$175,172,826</u>

EAGLE PACIFIC INSURANCE COMPANY
COMPARATIVE STATEMENT OF INCOME
FOR THE YEARS ENDED DECEMBER 31,

	<u>1996</u>	<u>1995</u>
<u>UNDERWRITING INCOME</u>		
Premiums earned	\$50,749,215	\$46,453,020
DEDUCTIONS:		
Losses incurred	24,817,305	24,441,265
Loss expenses incurred	10,793,341	9,185,510
Other underwriting expenses incurred	13,978,183	13,908,089
Total underwriting deductions	49,588,829	47,534,864
Net underwriting gain or (loss)	1,160,386	(1,081,844)
<u>INVESTMENT INCOME</u>		
Net Investment Income earned	7,421,236	7,469,141
Net realized capital gains or (losses)	1,494,717	4,073,877
Net investment income gain or (loss)	8,915,953	11,543,018
<u>OTHER INCOME</u>		
Net gain or loss		
from agents' or premium balances charged off	(385,750)	(325,000)
Finance and service charges		
not included in premiums	30,805	25,883
Miscellaneous interest income	33,236	(7,259)
Total other income	(321,709)	(306,376)
Net income before dividends to policyholders and before federal and foreign income taxes	9,754,630	10,154,798
Dividends to policyholders		
Net income before federal and foreign income taxes	9,754,630	10,154,798
Federal and foreign income taxes incurred	3,257,363	2,966,282
Net income	\$6,497,267	\$7,188,516

	<u>1996</u>	<u>1995</u>	<u>1994</u>	<u>1993</u>	<u>1992</u>
Surplus as regards policyholders, December 31, previous year	\$38,252,952	\$32,630,597	\$32,777,696	\$26,607,535	\$35,609,742
<u>GAINS AND (LOSSES) IN SURPLUS</u>					
Net income	6,497,267	7,188,516	4,524,426	6,277,186	6,013,579
Net unrealized capital gains or (losses)	91,012	191,338	(216,312)	(6,691)	(68,750)
Change in non-admitted assets	(1,257,288)	1,153,501	(721,213)	(67,258)	(835,845)
Change in provision for reinsurance	109,000	89,000	(234,000)	(33,076)	(111,191)
Capital changes					2,665,000
Surplus adjustments					(2,665,000)
Dividends to Stockholders	(3,700,000)	(3,000,000)	(3,500,000)		(14,000,000)
Changes in surplus	1,739,991	5,622,355	(147,099)	6,170,161	(9,002,207)
Surplus as regards policyholders, December 31, current year	\$39,992,943	\$38,252,952	\$32,630,597	\$32,777,696	\$26,607,535

NOTES AND COMMENTS TO FINANCIAL STATEMENTS

1. **BONDS** are stated at amortized cost using the scientific method. For mortgage backed structured securities, the Company uses prepayment estimates provided by Bloomberg CMO Analytics.
2. **COMMON STOCK** are at market value. The Company has no subsidiaries.
3. **REAL ESTATE** is recorded at cost and depreciated over its estimated useful life.
4. **CASH and SHORT TERM INVESTMENTS** are stated at amortized cost using the interest method.
5. **FOREIGN EXCHANGE FUTURES CONTRACTS** used for trading purposes are recorded in the balance sheet at fair value at the reporting date. Realized and unrealized changes in fair values and interest income relating to trading instruments are recognized in investment income in the period in which the changes occur. Fair value is provided by a reputable dealer.
6. **UNCOLLECTED PREMIUMS** have been presented net as to commissions, dividends, and suspense items with balances over 90 days excluded as an admitted asset.
7. **FUNDS HELD OR DEPOSITED WITH REINSURED COMPANIES, and FUNDS HELD BY COMPANY UNDER REINSURANCE TREATIES** are primarily attributed to a quota share (pooling) agreement with its affiliate, Pacific Eagle Insurance Company wherein Eagle Pacific Insurance Company assumes 100% of Pacific Eagle's writings and then retro-cedes 17.5%.
8. **UNPAID LOSSES AND LOSS ADJUSTMENT EXPENSES:**
The reserves carried by the Company for these liabilities were \$70,013,463 and \$10,688,053, respectively, as of December 31, 1996. These amounts appear to also include amounts for bulk and IBNR reserves for allocated loss adjustment expense. (See Comments and Recommendations 2)
9. **FEDERAL INCOME TAXES INCURRED** are allocated as if each affiliate filed a separate tax return.

ACKNOWLEDGMENT

The cooperation extended to the examiners by the officers and employees of the Company during the course of this examination is hereby acknowledged.

In addition to Larry A. Omdal, Examiner-in-Charge, Insurance Examiners, Leman McLean, CFE, CPA, FLMI and EDP Specialist, Peter Mendoza, Martin Severeid, Chief Property/Casualty Actuary, D. Lee Barclay, FCAS, MAAA, and Actuarial Assistant, Jim Antush, all from the Office of Insurance Commissioner, State of Washington, participated in the examination and preparation of this report.

State of Washington)
) SS.
County of King)

Larry A. Omdal, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

Larry A. Omdal
Examiner-in-Charge

Subscribed and sworn to before me on this _____ day of _____, 1998.

Notary Public in and for the
State of Washington,
residing at _____